

BILL ANALYSIS

C.S.H.B. 398
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Financial Institutions
Committee Report (Substituted)

BACKGROUND AND PURPOSE

Refund anticipation loans (RALs) are short-term, high cost loans secured and repaid by an individual's tax refund from the IRS.

The annual percentage rate (APR) for RALs range from 70 to 700 percent due to the numerous fees associated with RALs. Tax preparers and RAL lenders rarely report this rate to consumers. Instead, they report a lower rate which does not account for the fees associated with the loan. Tax preparers offering RALs engage in aggressive advertising campaigns during tax season, and at times mislead consumers about the available options. Brokers rarely make it clear to consumers that they can receive their refund from the IRS in as little as 10 days without utilizing these high cost, high risk loans. In many cases, consumers are not aware that they have taken out a loan.

RALs erode the benefits of the Earned Income Tax Credit for working Texans. During 2003, nearly two million Texas taxpayers received federal Earned Income Tax Credit refunds worth about \$3.8 billion. However, an estimated \$251 million of these public funds never reached the taxpayers. Commercial tax preparers received the majority of these funds, nearly \$166 million, assisting taxpayers in navigating the complex tax laws just to claim their earned benefits. The remaining \$85 million consisted of refund anticipation loans which allowed taxpayers to receive some, if not all, of their money approximately one week earlier than they would have without the loan.

C.S.H.B. 398 provides for the regulation of tax refund anticipation loans or checks with certain penalties.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the Consumer Credit Commissioner in SECTION 1 (Section 350.004, Finance Code) of this bill.

ANALYSIS

C.S.H.B. 398 amends Subtitle B, Title 4, Finance Code, as follows:

The substitute establishes restrictions on executing or processing RALs without complying with this chapter. It allows the commissioner to adopt rules as necessary to accomplish the purposes of this chapter.

The substitute requires that any entity which facilitates RALs register with the Office of the Consumer Credit Commissioner to ensure appropriate oversight. It also stipulates that the commissioner may set registration fees and penalties at the level necessary to cover the costs associated with implementing the registration and complaint procedures.

The substitute requires facilitators to post a bond in the amount of \$50,000 per location to pay damages and penalties to consumers harmed by violations of this Act. It allows companies to apply for a waiver of the bond requirement provided that they can demonstrate that the applicant has and will maintain net assets of \$25K (indexed to inflation). It also allows the net assets of the parent company to be counted toward this requirement provided that the parent company guarantees the performance and financial responsibility of the applicant. The substitute provides

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that a parent company may file a bond in an amount determined by the commissioner, not to exceed \$500K, to be effective for all of the parent company's franchise locations.

The substitute establishes procedures for registration and renewal for facilitators.

The substitute requires facilitators to disclose the refund anticipation loan rate in terms of the annual percentage rate for the RAL as established by the federal Truth in Lending Act. The substitute also requires facilitators to disclose the total amount of all fees associated with the RAL that are not included in the APR.

The substitute prohibits facilitators from arranging for fees for insurance, attorney's fees, or collection costs in association with the issuance of a RAL.

The substitute requires that RAL facilitators disclose the nature, costs and risks of the RALs. It also requires facilitators to inform the consumer of the average time by which the IRS reports that they can process the return.

The substitute allows for alternative disclosures to be approved for use by the commissioner provided that they are substantially the same.

The substitute prohibits certain misleading language in advertising, establishes size requirements for print advertising, and requires that the RAL not be advertised without a disclosure regarding the availability of electronic tax returns that may be obtained without taking out a loan.

The substitute prohibits RAL facilitators from engaging in debt collection for any RAL creditor. This is intended to address the practice of RAL agreements which allow creditors to take a consumer's tax refund and use it to pay back any prior RAL debts for any RAL lender.

The substitute requires RAL and RAC facilitators to file an annual report detailing the volume (in dollars) of RAL and RACs that they have facilitated, and the average loan period. It also requires facilitators to report the number of loans that are not paid in full from the consumer's tax refund.

The substitute authorizes the commissioner to impose penalties for violations of the bill beginning with a cease and desist order for a first offense, revocation or suspension of registration, and civil penalties for subsequent offenses. It also requires the state agency to establish a complaint procedure for consumers as well as gives consumers the ability to sue RAL and RAC facilitators for violations. The substitute provides for the prohibition of deceptive trade practices and private cause of action, including class action suits.

EFFECTIVE DATE

January 1, 2006

COMPARISON OF ORIGINAL TO SUBSTITUTE

C.S.H.B. 398 modifies the original by changing the definition of a facilitator in to ensure that it may not be construed to include companies that do not directly interact with customers in the RAL transaction, such as banks.

The substitute modifies the original by lowering the bond requirement required for facilitators from \$100K to \$50K. It also allows companies to opt for a net asset test of \$25K (indexed to inflation) in lieu of a surety bond and a parent company's assets to be used to fulfill the net asset requirement, including a blanket bond for all of their franchise locations not to exceed \$500K.

The substitute modifies the original by adding language that requires a facilitator to be a person authorized to provide tax filing services by the Internal Revenue Service. It also includes a provision authorizing the Consumer Credit Commissioner to adopt rules to allow for an expedited procedure to register additional offices for facilitators that are already registered with the state, and to allow registered facilitators to change the address on their registration. The

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substitute adds language to require the commissioner to make publicly available a list of all facilitators registered under this section.

The substitute modifies the original by changing the date of registration renewal to April 30th in order to match the tax cycle. It also makes technical changes to the language recommended by the commissioner.

The substitute modifies the original by extending the time period during which a facilitator may request a hearing from 5 days to 30 days after they have been informed that the commissioner has denied their application for registration. It also includes technical changes to the language in this section recommended by the commissioner.

The substitute modifies the original by eliminating the rate calculation formula and requires that the refund anticipation loan interest rate must be disclosed using the annual percentage rate for the borrower's refund anticipation loan using the guidelines established under the federal Truth in Lending Act (15 U.S.C. Section 1601 et seq.). Also, when disclosing the RAL rate, the facilitator must also disclose the total amount of all fees associated with the loan that are not included in the annual percentage rate calculation. The substitute also eliminates the maximum interest rate.

The substitute modifies the original by adding language that allows companies to have their own disclosures approved by the commissioner. The substitute requires the facilitator to insert the average time published by the IRS for E-file returns in their disclosure statements, disclosure of fees, consumer notification if the terms change with right of refusal.

The substitute modifies the original by adding language that requires a facilitator that is arranging for fees for cashing a check must inform consumers that if they have a bank account, their bank may cash the check without charging a fee.

The substitute modifies the original by adding language to include disclosures in Spanish as well as including language the taxpayer has a choice of methods for receiving a tax refund, and the lender must first disclose the availability and timing of receiving a refund directly from the IRS without incurring the cost of using a bank product before describing any available bank products.

The substitute modifies the original by removing language that proscribes certain collection actions and affiliations with check cashing enterprises. The substitute adds language that allows for an alternative application disclosure. The substitute adds language that new requirements for advertisements, including language that prohibits misleading information in RAL advertisements. It also requires RAL advertisements to disclose that the IRS e-file is available to the consumer without incurring the costs of a loan.

The substitute modifies the original by changing the date for the reporting periods. It allows for the creditor's best estimate of the average number of days for which refund anticipation loans facilitated by the facilitator were outstanding before being repaid by the IRS. The substitute adds the number of loans which are not repaid in full by the IRS as a requirement for the annual report.